IN THE

Supreme Court of the United States

October Term, 1941

No.———

A. W. Sewell and John Sewell ..... *Petitioners*

v.

J. E. Crosbie, Inc. (a Corporation) and
Henry H. Cross Company (a Corporation) *Respondents*

BRIEF OF PETITIONERS ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS EIGHTH CIRCUIT

STATEMENT OF FACTS

This joint action against respondents, alleging a conspiracy to defraud and damages suffered thereby, was brought in the Ouachita Chancery Court of Arkansas by Petitioners, residents of Illinois, against Respondent Henry H. Cross Co., also a resident of Illinois and J. E. Crosbie, Inc., a resident of Oklahoma. The action therefore is not one wholly between citizens of different states

and not removable if the action stated against respondents is joint.

28 U.S.C.A. 71

We have stated the facts of the case briefly in our Petition. We do not resummarize here. The question is whether a separable controversy is presented in the complaint filed in the State court and because of the fact that the complaint itself is decisive of the issue we here call further attention to certain allegations of the complaint.

The agreement of lease created between plaintiffs and respondent, J. E. Crosbie, Inc., a trust upon the part of Crosbie to faithfully account to the plaintiffs for the exact number of barrels of oil recovered and for their proportionate royalty interest in the true sale price of the oil; and that Petitioners at all times relied upon the good faith of J. E. Crosbie, Inc., to fulfill its obligation in this respect by marketing the oil at the highest price obtainable and by obtaining for plaintiff their full royalty interest in the true sale price of the oil produced (R. 8).

The complaint further alleged that J. E. Crosbie, Inc., acting in collusion with the purchaser of the oil (Henry H. Cross Company) and in furtherance of a scheme to cheat and defraud the plaintiffs had been selling the oil at a price substantially more than the price disclosed to the plaintiffs and substantially in excess of the price paid to the plaintiffs for their royalty oil; that J. E. Crosbie, Inc., and the purchaser of said oil (Henry H. Cross Company) fraudulently represented to plaintiffs that the oil was being sold and purchased at the price basis received by plaintiffs (Par. 14 & 16, R. 9-10).

The respondents J. E. Crosbie, Inc., and Henry H. Cross Company, by secret agreements and secret contracts, acting in collusion and in furtherance of a scheme to defraud and cheat Petitioners, have withheld from the Petitioners the true sale price of the oil (Par. 18, R. 10-11). The complaint further specifically alleged the violation of four separate and distinct provisions of Act 222 of the Acts of Arkansas of 1929 in the following particulars:

> (1) By entering into secret contracts between themselves whereby J. E. Crosbie, Inc., received a greater price per barrel than that paid to plaintiffs for their proportionate royalty in the same oil.
>
> (2) By not disclosing to the plaintiff that J. E. Crosbie, Inc., was being paid a higher price than plaintiffs for the same oil.
>
> (3) By not disclosing to these plaintiffs that other royalty owners similarly situated to the plaintiffs were also being paid a higher price than plaintiffs for the same oil.
>
> (4) By failing to protect the royalty interest of these plaintiffs in not paying such plaintiffs the same price for oil as that procured and paid to J. E. Crosbie, Inc., for the same oil.

That said acts, violations and breaches of duty on the part of the defendants were done and committed in the knowledge that these plaintiffs were being discriminated against in the price paid them for their royalty portion of this oil (Par. 19, R. 11-12).

THE PRAYER

Plaintiffs pray for a full accounting, and that upon final hearing for a decree in judgment against the defendants jointly and severally, for all sums lawfully due them together with statutory penalties provided in Act 222 of the Acts of Arkansas of 1929 for costs and for all other proper relief to which the plaintiffs are entitled (Par. 11, R. 12).

The answer of the Henry H. Cross Company when filed contained the admission that from April 1, 1929, to September 15, 1930, there was paid to J. E. Crosbie, Inc., 10c per barrel for its seven-eighths interest in the oil more than was paid to the plaintiffs for their royalty oil (R. 43). The answer of the Henry H. Cross Company further admits that between September 16, 1930, and January 31, 1938, it paid J. E. Crosbie, Inc., 5c per barrel for its seven-eighths working interest more than was paid to plaintiffs (R. 43-44). We point out here that all of the oil produced on this lease was sold and delivered to the purchaser, Henry H. Cross Company, without any separation of the royalty interest oil from the working interest oil, i.e., all of the oil was commingled and unseparated when delivered into the pipe lines of the Henry H. Cross Company.

Petitioners contend:

(1) That the complaint filed in the state court was clearly a joint cause of action for conspiracy against both defendants from which no separable controversy can be carved.

(2) That the Federal District Court acquired no jurisdiction upon the petition of removal except to sustain Petitioners' motion to remand.

(3) That all proceedings in the District Court following Petitioners' motion for remand were mere nullities.

(4) That the Circuit Court of Appeals erred in affirming the decree of the District Court in retaining jurisdiction of the cause.

ASSIGNMENT OF ERRORS

(1) The District Court erred in assuming jurisdiction over this cause and in overruling Petitioners' motion to remand to the state court, and the Circuit Court of Appeals erred in affirming the action of the District Court in retaining jurisdiction.

ARGUMENT

The majority opinion of the Circuit Court of Appeals asserts the existence of a separable controversy in the complaint in the following language from the opinion:

> "The complaint clearly charges the defendant J. E. Crosbie, Inc., with a breach of contract in failing to account to plaintiffs for the correct proceeds of oil sold on their behalf. This cause of action was necessarily one in which only the plaintiffs and the defendant J. E. Crosbie, Inc., were involved" (R. 82).

We therefore limit our endeavors to an effort to show that the breaching of the lease contract and the failure to account on the part of J. E. Crosbie, Inc., was part and parcel of the conspiracy between both defendants and when considered, as it should be, along with all other allegations in the complaint, that it does not present a controversy separable from the conspiracy allegation, the conspiracy being the one distinct primary subject of controversy against both defendants.

The majority opinion completely ignores the provisions of Act 222 of the Arkansas General Assembly, 1929, and the allegations of the complaint which also charge the purchaser of the oil with the direct responsibility of accounting and paying to the plaintiffs, royalty owners, the correct sums due.

Section 1 of Act 222 of the Acts of Arkansas of 1929 provides:

> "All purchasers of oil and gas shall pay to the royalty interest the same premium or bonus as the purchase price to the lease holder or working interest under any oil or gas or mineral lease on lands from which oil or gas may be purchased under contract with the lease owner or operator."

Section 5 of said Act provides:

> "It shall be the duty of any purchaser of oil or gas to pay the royalty interest at the same time it pays the lessee or producer."

One of the writers of this brief was a member of the Arkansas House of Representatives when Act 222, *supra,* was passed. It is apparent from the language of the Act that the Legislature knew that royalty owners as a group were not engaged in the oil business, probably would not know how to test the grade and quality of crude oil if furnished with the proper laboratory, and in a great number of instances, lived long distances away from the oil producing lands. In this case, Petitioners lived a distance of over 800 miles from these oil producing lands. The Legislature knew that the average royalty owner is completely at the mercy of his lessee. The Legislature wisely concluded that such a situation might be an invitation to a conspiracy to defraud between the lessee and the purchaser of the oil and for that very reason, Act 222 was passed for the protection of the royalty owners in their rights. Certainly, the Act was dictated by the wisest public policy in an effort to minimize fraud.

It must be conceded that the one distinct primary subject of controversy presented by Petitioners' original complaint filed in the State Court was the allegation of conspiracy against both defendants to the damage of Plaintiffs.

> "If the facts alleged in a declaration, complaint, or petition show but one distinct primary right on the part of plaintiff, and one delict or wrong on the part of defendant involving that right, there is but one cause of action stated. This is true, although incidental matters are alleged in connection with the pri-

mary right, which render other parties than the main defendant proper or necessary to the litigation, or although facts are stated which, while germane to the primary purpose of the action might constitute independent grounds of relief; and where a single transaction is relied on, the complaint does not necessarily state two causes of action, because the facts alleged may show a liability both in contract and in tort. It is not necessary that the wrong shall consist of a single act, or that the resulting injuries consist of but a single element; and the amount sought to be recovered may be made up of several items. The complaint may, without stating more than one cause of action, set forth different grounds or theories upon which plaintiff is entitled to the same relief, or may set forth different means or methods employed in accomplishing the same wrong." 1 *C. J.* 1056-1057.

The above quotation has been cited with approval by the Eighth Circuit Court of Appeals.

Tabor v. *Universal Exploration Company,*
48 F. (2d) 1047.

See also:

Pirie v. *Tvedt,* 115 U. S. 41;

Torrence v. *Shedd,* 144 U. S. 527;

McCandless v. *Furlaud, et al,* 296 U. S. 140;

Fordyce v. *Dix,* 58 Ark. 136, 23 S.W. 767.

Ordinarily conspiracies in their operation may be likened to wheels, the acts of the various co-conspirators furnishing the supporting spokes.

It must be apparent to this Honorable Court that however evil the intentions of a clever and cunning lease opera-

tor, while standing in a position of trust toward his unsuspecting royalty owner, he could commit no breach of his lease agreement in the sale of the oil by a fraudulent conspiracy to defraud the royalty owners until he found a purchaser, ready and willing to enter into the scheme of fraud and deceit. In this case Henry H. Cross Company was that purchaser, an active co-partner in the fraud. Without the affirmative acts of Cross, or some other purchaser ready and willing to play the same part, the complaint fails to state an action against anyone. Under such circumstances certainly no separable controversy is presented.

The lease imposed an obligation upon J. E. Crosbie, Inc., the lessee, to faithfully account to Petitioners and Act 222 *supra* placed the same obligation of a proper accounting to Petitioners squarely upon the purchaser, in this case Henry H. Cross Company. The complaint did not allege that the defendant Crosbie had paid the additional sums due Petitioners to J. E. Crosbie, Inc. In fact, the answer of the Henry H. Cross Company reveals that Henry H. Cross Company is still withholding the additional sums due these Petitioners. In drawing the complaint, Petitioners had been refused access to the records of either of the defendants and did not know in fact which of the defendants had in its possession the additional sums due Petitioners. The prayer for a joint accounting from both defendants was entirely proper as was the prayer for a joint recovery of both defendants for the total damages by Petitioners because of the conspiracy alleged.

Parties to an unlawful agreement to defraud are liable in Arkansas, as joint tort-feasors to the extent of the damage done as a result of the conspiracy. The liability of a party conspirator does not depend upon the

extent to which he profited by the conspiracy nor upon the extent of his activity in it. It is sufficient to establish liability that the party sued was a party to the conspiracy.

Wilson v. *Davis,* 138 Ark. 111, 211 S. W. 152.

The Eighth Circuit Court of Appeals has announced the same rule in a case originating in Arkansas.

United Mine Workers of America, et al v. *Coronado Coal Co., et al,* 258 Fed. 829, 830.

Other jurisdictions also so declare the law.

"Each conspirator is jointly and severally liable for all damages resulting from the conspiracy."

Louis v. *Ingram,* 57 Fed. (2d) 463. (10th C.C.A.)

When there is a general scheme to defraud, all parties are held to account.

McCandless v. *Furlaud, et al.,* 296 U. S. 140, 56 S. Ct. 41.

The complaint charged both defendants with this conspiracy and they are both jointly accountable and jointly liable to petitioners for the full extent of their damage.

When a purchaser buys property under fraudulent circumstances and with knowledge of the rights or interest of the person being defrauded, such purchaser is turned into a trustee and such purchaser and vendor are held to a joint rigid accountability to the person defrauded.

Drake v. *Thyng,* 37 Ark. 228.

The majority opinion of the Circuit Court of Appeals states:

"* * * That a joint accounting is demanded cannot affect the separability of the controversy between the plaintiff and defendant, J. E. Crosbie, Inc., over its alleged failure to pay over to them what, by the terms of their contract, they were lawfully entitled to receive. *Chicago & A. R. Co.* v. *New York, L. E. & W.R. Co.*, 24 F. 516-517" (R. 83).

We have examined this case and find that it did not originate in Arkansas, it did not involve an alleged conspiracy to defraud; it did not involve the sale of trust property or sale of anything. It was an action to restrain defendants from violating the conditions of several contracts and was for an accounting for monies due the plaintiffs. In fact in this case, relied on by the Circuit Court of Appeals, the liability, if any, on the part of each defendant was separate and distinct and the court held that there was nothing in the agreement sued on to imply that the defendants were sureties for each other. Each accounting from each of the defendants depended entirely upon a different set of facts and circumstances in fact entirely different subject matter, and the court quite properly held that there was nothing joint about the accounting sought from the defendants. We quote from the opinion at page 517:

"One cause of action against the defendants is founded upon the alleged breach of the second clause of the agreement, Exhibit A., annexed to the bill, whereby each defendant convenants to make good any deficiency in the earnings of plaintiff necessary to pay plaintiff interest upon its issue of mortgage bonds in the proportion to which each defendant may respectfully receive gross earnings accruing from its traffic with the plaintiff. The undertaking thus expressed is not a joint one on the part of defendants, but is several and distinct by each, and the liability of each is measured by its own proportion of gross earn-

> ings received from its traffic with plaintiff. There is nothing in the agreement that implies that the defendants are to be sureties for each other or answerable for each other's default."

Plainly the only accountability of the defendants in the above case was based upon the traffic that each particular defendant had with the plaintiff.

Each account therefore was a completely separate and distinct business enterprise. There is not the remotest analogy in the case of *Chicago & A. Ry. Co.* v. *New York, L. E. & W. R. Co.* (C. C.), 24 F. 516, 517, to the instant case for the reason that the Sewells brought suit for a conspiracy and both defendants were engaged in handling the same identical barrels of oil belonging to these plaintiffs, and under the law of Arkansas, as announced in *Wilson* v. *Davis, supra,* both defendants are jointly liable to the Sewells for the amount of their damage.

The majority opinion of the Circuit Court of Appeals states that the instant suit is substantially similar to that of *Hamilton* v. *Empire Gas and Fuel Company* (8 Cir.), 297 F. 422. This case is clearly distinguishable from the instant case for the following reasons:

(1) It did not arise in Arkansas.

(2) It did not involve any claim with reference to the sale of oil from a lease, which is the sole subject matter of the instant suit.

(3) It did not involve or allege concealment and misrepresentation on the part of the defendants in the furtherance of a scheme to defraud plaintiff, as is alleged in the instant suit.

(4) It was not a suit for an accounting from any of the defendants, whereas the instant suit is for a joint accounting upon identical liability of all defendants.

(5) No violation of a local statute was claimed, as is alleged in the instant case which places identical responsibilities upon the defendants in connection with the disposition of plaintiffs' oil.

(6) It was not an action for deceit as is the instant case.

(7) The resident defendants were employees of the non-resident defendant. The action was for failure to develop the oil properties, non-feasance. The resident defendants under such a charge were neither necessary nor proper parties to the action, whereas in the instant case, the defendant Henry H. Cross Company actually bought the oil and actually induced and participated in the conspiracy to defraud the plaintiffs.

Under the opinion in *Hamilton* v. *Empire Gas and Fuel Company, supra,* it is stated at page 425:

> "It may be conceded that, if the individual defendants, through conspiracy or otherwise procured the defendant company to breach its contract, the individual defendants would be liable."

Here Cross is charged with inducing the conspiracy and participating in it. Before Crosbie could breach its lease obligation to these Petitioners in the manner set forth in the complaint, by conspiracy and deceit, it had, of necessity, first to find a purchaser, a purchaser ready and willing to violate the provisions of Act 222, and ready and willing to send out false statements to the royalty owners and ready and willing to connive with Crosbie to prevent the royalty owners from discovering the true

facts. If Henry H. Cross Company had performed its obligations in paying the royalty owners the same price as that paid to Crosbie, there would be no suit; if Cross had furnished correct and true statements each month to the royalty owners, revealing the additional sums being paid to Crosbie, there would be no suit. In short, the success of the breach of the lease obligation on the part of Crosbie depended absolutely upon the cooperation of the purchaser in the general conspiracy to defraud and to violate the provisions of Act 222. We insist again that Crosbie could not possibly market the royalty oil for our credit, until a purchaser was found, regardless of whether the oil was being sold for a proper or improper sum. In this case Cross apparently stood to receive a substantial profit by the success of the scheme as to this date it still has in its possession the funds lawfully due these Petitioners. The following language from the dissenting opinion of Mr. Justice Woodrough is significant:

> "On the argument at the bar Crosbie's counsel frankly conceded that the plaintiffs had tried to plead a joint cause of action against both defendants and there is no claim that there was any sham or fraudulent joinder. That being so, I would indulge every fair intendment to sustain the pleading as a whole in accord with its intention, and going at it in that way, it seems reasonably clear to me that the plaintiffs charged and relied for their recovery on more than a mere failure of Crosbie to account for the correct proceeds of oil sold on plaintiffs' behalf. They relied rather on the joint action of both defendants cooperating to accomplish a concealment of the facts concerning the disposition of the oil production and consummation of actionable deceit whereby plaintiffs were defrauded of their royalty rights. Therefore it seems to me the case is not analogous to *Hamilton* v. *Empire Gas and Fuel Co.*, 8 Cir., 297 F. 422. * * *" (R. 85).

WHETHER A SEPARABLE CONTROVERSY IS PRESENTED MUST BE DETERMINED BY LOCAL LAW—IN THIS CASE BY THE LAW OF ARKANSAS

Alabama Great So. R. R. Co. v. *Thompson,*
200 U. S. 206;

Erie Railroad Co. v. *Tompkins,*
304 U.S. 64-92, 82 L. Ed. 1188;

Watson v. *Chevrolet Motor Co.,*
68 F. (2d) 686 8th Circuit;

Cert. Denied 56 S. Ct. 716, 292 U. S. 637.

The Watson case, *supra,* is only one of many cases decided by the Eighth Circuit Court of Appeals holding that any question of separable controversy must be determined by local law.

Leonard v. *St. Joseph Lead Co., et al,*
75 F. (2d) 390;

Culp v. *Baldwin,* 87 F. (2d) 679.

See also Paragraph 4 Sec. 1084 *Simpkins Fed. Practice* (1938).

The decisions are uniform and we do not further belabor the Court with cumulative authorities.

Under the law of Arkansas, the complaint stated an action for conspiracy against both defendants and the action is joint. The case of *New Amsterdam Casualty Company, et al.,* v. *State,* 121 S.W. (2d) 75, 196 Ark. 1092, is a conspiracy case strikingly similar in facts to the instant case. The first headnote of this case follows:

(1) Conspiracy, Key 18.

"Evidence that state's purchasing agent, who was under duty to sell state's cotton on competitive bids to the best advantage of the state, permitted cotton broker to sell the cotton, that broker sold cotton for higher price than false bids indicated, that broker had purchasers issue two checks, one to the state for the amount of false bid and one to broker for difference between false bid and actual price received, sustained court's finding of conspiracy between purchasing agent and brokers to defraud the state."

In *New Amsterdam Casualty Company, et al.* v. *State, supra,* practically the identical means were employed in furtherance of a conspiracy to defraud. False statements were prepared, a secret and separate remittance was made to the broker and there was the actual sale of the product for a higher price than that revealed to the state.

Plainly the owners of the royalty in the instant case, who were the victims of the same kind of conspiracy and who have set the facts up fully in their complaint, have stated a joint action under the Arkansas law against both defendants for conspiracy.

"A conspiracy is a combination of two or more persons by concerted action to accomplish a criminal or unlawful purpose or some purpose not in itself unlawful, by criminal or unlawful means."

Pettibone v. *U. S.*, 148 U. S. 197.

"Conspiracy consists of a combination and agreement of two or more persons to do some illegal act; or a combination and agreement to affect a legal purpose by illegal means."

Clinton v. *Estes*, 20 Ark. 224.

It will be necessary for this Honorable Court and the Supreme Court of Arkansas to redefine what constitutes a conspiracy to defraud before our complaint can be prevented from stating such an action. The charge of conspiracy in the complaint is so clear and plain that it cannot be escaped, even though we do not invoke the rule of indulging all reasonable intendments of the pleading in favor of the pleader.

Henry H. Cross Company was not an innocent purchaser of this oil. Act 222 of the General Assembly of 1929, charges the purchaser with full notice as to the ownership and rights of the parties. The Arkansas Supreme Court has also determined that the purchaser of oil is charged with notice of the royalty owner's interest in the title to the oil purchased.

Shreveport Pipe Line Company v. *Bennett,*
172 Ark. 804, 290 S.W. 929.

> "Under crude oil purchasing contracts with the lessee, the law creates a privity of interest between the purchaser and the lessor or royalty owner; such purchaser of the working interest oil is under an implied obligation to take and pay for the royalty oil also. It is a general principle that such payments should be made without any discrimination against the landowner, that is, at the same contract price. Arkansas, by statute has provided that purchasers must pay the same price for royalty oil (including any premiums or bonuses provided by contract) as paid to the producer."

Glassmire, Second Edition, 1938, *Oil and Gas Leases and Royalties.*

The complaint charges the breaching of a trust fiduciary relationship on the part of Crosbie and the complaint

sets out the details of the manner in which Henry H. Cross Company induced the breach and participated in it.

> "Trusts are not only enforced against those persons who are rightfully possessed of trust property as trustees, but against all persons who come into possession of the property bound by the trust with notice of such trust. Even a purchaser still more a volunteer taking possession of trust property with notice of the trust will be made a trustee by the court."
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> 26 R. C. L. 1237.

> "If parties are interested together by mutual agreement, neither party can exclude the other from what was intended for the common benefit; and any private benefit touching the common right which is secured by either party, will turn him into a trustee for the benefit of both or all."
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> 16 R. C. L. 903.

We confess that we are at a complete loss to understand the retention of this case in the federal court without the citation of a single Arkansas case to support such action, and especially when the law of Arkansas controls.

The majority opinion of the Circuit Court of Appeals ignores the Arkansas law and is repugnant to all of the Arkansas decisions which are applicable to the issues here presented. This case involved substantial sums of money. Counsel for respondents are able members of the bar. They could not find nor did they produce in their briefs or in their argument before the Circuit Court of Appeals, a single Arkansas case touching the question of whether, under the Arkansas law, this complaint here on review presents a separable controversy. The majority opinion of the Circuit Court of Appeals, in its unwarranted departure

from the applicable decisions of this Court, has rendered an opinion which offends the law of the State of Arkansas, and an opinion which likewise offends the decisions of this Honorable Court.

We earnestly submit the lower District Court erred in refusing the motion of Petitioners to remand this case to the state court, and that the Circuit Court of Appeals, by the majority opinion, erred in affirming the decree of the lower District Court, and that, therefore, this Court should grant a writ of certiorari to the United States Circuit Court of Appeals for the Eighth Circuit.

Respectfully submitted

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